Goodmans LLP

Planning for an IPO in Canada

An initial public offering (IPO) can represent a significant opportunity for a company. An IPO attracts funding, liquidity and publicity but also significant regulatory requirements and expense. Below are some of the key considerations and steps a company should take early on to prepare for an IPO and maximize its chances of success.

1. Establish an Expert Team

A team of external experts is needed for any IPO. Some of the key members of this team include:

a. ***Legal Counsel.*** A company's legal counsel can help assemble the external team and navigate the IPO process. It will negotiate the underwriting agreement with your investment banks and their legal counsel, draft the prospectus, oversee the regulatory review by the securities regulators and stock exchanges, coordinate due diligence and close the IPO. Law firms with deep capital markets experience have established best practices for completing successful and timely offerings.

b. ***Investment Banks.*** IPOs are usually underwritten by a lead investment bank along with one or more additional investment banking syndicate mem bers. The lead investment bank will manage and help to assemble the syndicate, assist with drafting the prospectus, conduct financial due diligence on the business, prepare marketing materials, assist with the road show and lead other selling efforts. The investment bank should know the company's industry and the key investors to target for the IPO. The investment bank must also be committed to the IPO timeline and have the necessary resources to underwrite the offering and provide after-market trading support and research analyst coverage. There should be agreement as to the approach for valuing the company and promoting it to investors. The chosen underwriter's reputation will significantly impact the IPO's outcome.

c. ***Accounting Firm.*** The selected accounting firm will audit or review the financial statements included in the prospectus, deliver an audit opinion on the financial statements, review other financial disclosure and provide comfort letters required for the offering. Suitable auditors are experts in the company's industry, willing and able to work within the timeline for the IPO and trusted by potential investors. The accounting firm can also help the company's financial team implement internal controls and processes for the IPO and for operating as a public issuer afterwards. An accounting firm should be retained early on to avoid potential delays that can arise in preparing the required financial disclosure.

2. Select a Stock Exchange

The choice of stock exchange will often turn on the company's size and stage of development. The Toronto Stock Exchange (TSX) is Canada's largest marketplace requiring that prospective listing companies meet the highest financial and distribution thresholds. Other Canadian exchanges include the TSX Venture Exchange, the Canadian Securities Exchange and the Aequitas NEO Exchange, which have lower thresholds and less burdensome requirements. It is often prudent to meet with the chosen stock exchange in advance of an IPO to socialize the possibility of listing the company on the exchange.

3. Build out the Company's Financial Reporting Team

A company's CFO will play an important role in the IPO. The CFO will be expected to deliver accurate financial information to the public and investors will need to be comfortable with the competency and experience of the CFO before investing in the Company. The CFO should have public company experience or be willing and able to learn the complexities of going public and operating as a public company.

A company going public can also benefit from an experienced controller to maintain internal control and accounting standards that meet the requirements of applicable securities laws. Where resources permit, it may also be prudent to hire additional accounting staff to prepare for life as a public company and satisfy the continuous disclosure requirements once the company becomes a reporting issuer.

Securities and corporate laws also require public companies to have an audit committee consisting of at least three independent directors who are financially literate, subject to certain exceptions. The audit committee will play an important role in overseeing the company's financial reporting.

4. Prepare for Due Diligence

It is prudent to gather and organize diligence documents (such as incorporation documents, material contracts and documents relating to the issuance of debt and equity) early on in the IPO process to allow due diligence to be conducted in an efficient manner. The company's legal counsel can provide a sample checklist to guide the diligence and a data room can be used to store and organize company documentation. Doing this in advance will help identify missing or inadequate documentation and can expedite the IPO process.

5. Develop the Marketing Story

Early in the IPO process it is imperative that senior management work with the advisors to develop the key messages or investment highlights that will be communicated throughout the IPO marketing process, which would include industry highlights, the company's competitive positioning, the company's growth strategy and the proposed use of IPO proceeds. These messages should be presented consistently throughout the prospectus and all IPO marketing materials.

While developing the key messages consideration should be given to the key financial or operating metrics that will form the basis of the disclosure, and whether any non-GAAP measures or forward-looking information may be required as part of the marketing process. While non-GAAP measures and forward-looking information can be helpful for potential investors, they are highly scrutinized by regulators and care must be taken to ensure their use complies with applicable law.

Canadian securities laws require that any information used in marketing the IPO be included or derived from the prospectus thereby attracting liability in the event that such information contains a misrepresentation so it is important that the company carefully review these materials to ensure they are accurate.

6. Establish a Public Company Infrastructure

Before embarking on an IPO, a public company infrastructure needs to be established.

a. ***Corporate Governance.*** Any company going public should ensure its management team and board composition meet legal requirements, governance standards (e.g., those provided by Institutional Shareholder Services and Glass Lewis), and market expectations. Public company boards are generally expected to have a majority of independent directors or to explain how they will ensure independent decision-making. Moreover, the board should not have any gaps in knowledge or experience necessary for effective company oversight. The company's legal counsel and investment bank can assist in this review and help to establish a robust governance structure.

b. ***Executive Compensation.*** Director and officer compensation should be sufficient to attract and retain competent individuals. Existing equity compensation plans may need to be amended to account for the IPO and new plans can be implemented at the time of the IPO. The company's legal counsel can ensure the equity compensation plans comply with applicable stock exchange rules.

c. ***Policies.*** A public company should adopt policies relating to insider trading, disclosure, whistleblowing, committee/board charters, position descriptions and codes of conduct. The company's legal counsel can prepare forms of the various policies for the internal team to implement before or shortly following closing of the IPO.

d. ***Accounting.*** Continuous disclosure requirements imposed on public companies require early planning. Practices needed for timely reporting should be implemented before the IPO so that after the company is public, it is equipped for things like rapid closing of the books and quarterly conference calls. Auditors can help formulate and introduce internal controls and best practices.

e. ***Investor Relations.*** Before trading begins, it is often prudent to employ an investor relations firm. These firms can assist in the preparation of marketing materials and news releases, help set up the company's website including an investor relations section, handle communications with investors and assist with continuous disclosure responsibilities following closing of the IPO. Information disclosed to the public must be accurate and accompanied by proper disclaimers. The company's legal counsel can provide guidelines for management and staff to comply with securities regulations. In particular, there must be consistency between statements presented on the company's website, made during the roadshow and included in its prospectuses and continuous disclosure filings.

The Path to a Successful IPO

These steps can help lay the foundation for a successful IPO and avoid many potential pitfalls that can occur along the way. In addition to raising funds and gaining public exposure, the process can be an opportunity to improve the company's operations and governance, and establish a strong team of external advisors.

About Goodmans

Goodmans is internationally recognized as one of Canada's pre-eminent business law firms. Based in Toronto, the firm has market-leading expertise in M&A, corporate and transaction finance, private equity, restructuring, real estate, tax, litigation and other business-related specialties.

The firm represents a broad range of Canadian and foreign clients from entrepreneurial businesses to multinational corporations, financial institutions, pension funds and governments and has a reputation for handling challenging problems, often international in scope, which demand creative solutions.